Franchise Tax Board

SUMMARY ANALYSIS OF AMENDED BILL

Author: Hollingsworth & Soto, et al. Analyst: Darrine Distefano Bill Number: SB 438

Related Bills: See Prior Analysis Telephone: 845-6458 Amended Date: 02/04/04

Attorney: Patrick Kusiak Sponsor:

SUBJECT: Disaster Loss Deduction/Excess Loss Carryover/Los Angeles, San Bernardino, Riverside, San Diego, & Ventura County Fires

X DEPARTMENT AMENDMENTS ACCEPTED. Amendments reflect suggestions of previous analysis of bill as amended January 12, 2004.

___ AMENDMENTS IMPACT REVENUE. A new revenue estimate is provided.

___ AMENDMENTS DID NOT RESOLVE THE DEPARTMENT'S CONCERNS stated in the previous analysis of bill as introduced/amended ______________________.

___ FURTHER AMENDMENTS NECESSARY.

___ DEPARTMENT POSITION CHANGED TO ______________________.

X REMAINDER OF PREVIOUS ANALYSIS OF BILL AS AMENDED January 12, 2004. STILL APPLIES.

X OTHER - See comments below.

SUMMARY

This bill would allow taxpayers special tax treatment, called disaster loss treatment, for losses sustained as a result of the Southern California wildfires, losses related to the wildfires, and the San Simeon earthquake and related casualties.

This bill would also provide an allocation to local agencies from the state for financial assistance to repair or rebuild real property related to government services. This analysis will not address these changes to the Government Code, as they do not impact the department or state income tax revenue.

SUMARY OF AMENDMENTS

The February 4, 2004, amendments:

- Add a principal author and several co-authors to the bill,
- Add casualties related to the wildfires, and
- Add damage that occurred as a result of the San Simeon earthquake and related casualties to the list of disasters under the Personal Income Tax Law and the Corporation Tax Law.

The February 4th amendments resolve the department's technical considerations with respect to the bill as amended January 12, 2004. The amendments do not impact the department's operations. The amendments also do not affect the original revenue estimate provided in the department's January 12th analysis because the original estimate anticipated these amendments and included both the casualties related to the wildfires and the San Simeon earthquake. The revenue estimate is provided below for the author's convenience. The remainder of the department's analysis of the bill as amended January 12, 2004, still applies.

Board Position:			Legislative Director	Date
___ S	___ NA	___ NP		
___ SA	___ O	___ NAR	Brian Putler	2/19/04
___ N	___ OUA	X PENDING		

POSITION

Pending.

ECONOMIC IMPACT

Revenue Estimate

Based on the discussion below, the revenue losses from this bill are as follows (assumes fast track legislation enacted before April 2004):

Estimated PIT Revenue Impact SB 438 as Amended February 4, 2004 (In Millions) Fiscal Year Impact			
2003-2004	**2004-05**	**2005-06**	**2006-07**
Minor loss	-$5	-$9	-$4

Minor = Less than $500,000

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this bill.

Revenue Discussion

The impact of this bill would depend on the amount of disaster losses carried back, carried forward at 100% instead of 60%, and the amount of carryover losses deducted in subsequent years.

The estimated losses were determined in several steps. First, it is assumed that the special disaster loss treatment provided in this bill would be for losses sustained as a result of the Southern California wildfires, the expanded wildfire disaster coverage, and the San Simeon earthquake. Second, the total amount of damages for the Southern California wildfires was estimated to be $2.8 billion and the total amount of damages from the San Simeon earthquake was estimated to be $34 million in private losses.

It is estimated that approximately 20% of fire damage and 90% of the earthquake damage would not be reimbursed by insurance coverage for a total deductible loss of $590 million ($2.8 billion x 20% + $34 million x 90% = $590 million).

In order for a taxpayer to calculate the amount of disaster loss that can be deducted, the taxpayer uses three factors. First, the loss must be limited to the basis of the property (cost of the property plus cost of any improvements minus deductions such as depreciation). Second, any insurance proceeds or reimbursements must be deducted. Third, the taxpayer subtracts 10% of their federal adjusted gross income (AGI). The remaining amount is the disaster loss that can be claimed by the taxpayer. Using the department's disaster loss model, after applying qualifying losses for AGI and basis limitations of $147 million and an estimated first year usage of $148 million (historical use of similar losses under current law), it is projected that $250 million in losses would be allowed to be carried forward under the bill ($590 million - $147 million - $148 million = $295 million).

At a 6% average marginal tax rate, the total revenue loss over a period of a few fiscal years is estimated to be approximately $18 million, all attributable under the Personal Income Tax Law (PITL) ($295 million x 6% ~ $18 million).

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